



# Tax Information Bulletin

## STATE BOARD OF EQUALIZATION

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March 2001

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## What's Inside

### 1. Report It Right — Avoid the Dreaded Amended Return

Read this article if you have questions about reporting requirements related to the January 1, 2001, tax decrease.

### 2. Let's Settle the Matter

You may be able to settle a disputed tax billing or refund amount.

### 3. Drop Shippers Can Be Liable for Tax

Find out why and learn about a new way to figure out your tax liability.

### 4. Sales and Social Clubs and Fraternal Organizations

Did you know tax may apply to some of your food sales?

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This article clarifies the "relief of late payment penalty" on installment payment agreements.

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. . . it isn't fair to those who do. Our Investigations Division looks at and tackles taxpayer fraud.

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Some sellers hold only a few sales each year and must have a permit. Tax reporting requirements for those sellers have changed.

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## 1. Reporting Instructions for the January 1, 2001, ¼% Sales and Use Tax Decrease

*The following article explains how to complete Schedule BOE-531-T (Tax Adjustment Worksheet). Some filers receive Schedule TE instead of Schedule T, and some of the adjustments discussed in this article may not apply to the Schedule TE. — Editor*

We recently notified businesses about the tax rate decrease that took effect January 1, 2001. Since then, we have received inquiries regarding specific reporting issues and as a result have prepared the following questions and answers to help businesses complete their returns.

We have also prepared a more comprehensive question and answer list and another special notice on this subject, both of which are available on our website, [www.boe.ca.gov](http://www.boe.ca.gov), or through the Information Center's fax-back system, 1-800-400-7115.

### Q. I received a Tax Adjustment Worksheet with my return. Do I need to fill it out?

You must complete and return this worksheet (Schedule BOE-531-T) if you are reporting

- Sales or purchase transactions that occurred before the January 1, 2001, tax rate change. For example, fiscal year filers whose reporting period is from July 1, 2000, to June 30, 2001.
- Sales that occurred after the January 1, 2001, tax rate change, but you collected a

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higher tax rate and did not refund the excess to your customer.

- Sales or purchases of Section 6377 Manufacturer's Exemption and Section 6378 Teleproduction Equipment that occurred before the January 1, 2001 state tax decrease.
- Tax recovery deductions for transactions that occurred before the January 1, 2001 tax rate change. Tax recovery deductions include amounts that are reported on lines 10(a) through 10(d) (bad debt losses, tax-paid purchases resold, returned taxable merchandise, cash discounts).
- Rental receipts from leases of Mobile Transportation Equipment (MTE) if (1) you have elected to report based on fair rental value, and (2) the MTE was leased prior to January 1, 2001.

If you are not reporting any of the above items, you do *not* need to complete or return Schedule T.

**Q. I didn't reprogram my cash registers in time for the tax rate change and for a week I collected tax at the old rate. I refunded the ¼% tax amount only to customers who came back and requested a refund. How do I report the remaining excess tax collection to the State?**

You must separately report the transactions on Schedule T. Report the sales for which you *did* return the excess tax to your customer on Line 1 in Column B. Report the sales for which you did *not* return the excess tax to your customer on Line 1 in Column A. Also, please write a note in the margin of Schedule T identifying the amount on Line 1, Column A that represents sales where the higher tax rate was charged in error.

**Q. I have a bad debt to report. The original sale was made in 2000, but I'm writing it off my books in 2001. Which column do I use on Schedule T?**

You should enter the amount of the bad debt in Column A of Schedule T. By using Column A, your return will be credited the tax rate that was in effect when you made and reported the original sale.

**Q. My customer is returning merchandise that was purchased in 2000. What tax rate should I refund?**

You should refund the tax rate that was in effect at the time you made the original sale. When you complete your sales and use tax return, you should also fill out Schedule T so that your return will be credited the same amount of tax that you refunded your customer.

Remember, you can take a Returned Taxable Merchandise deduction only if

- You returned or credited to your customer the full sales price, including the actual amount charged as "sales tax," and
- The customer, in order to obtain the refund or credit, is not required to purchase other property at a price greater than the amount charged for the property returned.

**Q. What if I refunded tax based on the lower tax rate that took effect on January 1, 2001?**

You cannot take a Returned Taxable Merchandise deduction for merchandise returns for which you did not refund the entire sales price of the item — including all the amount originally charged as "sales tax."

## **2. Would You Like To Settle a Disputed Tax Liability or Refund?**

If you have a disputed civil tax or fee matter with the Board that you would like to settle, you may offer to settle for an alternative amount. As explained later in this article, staff may accept or reject your offer, or they may negotiate a different settlement figure.

**Who is eligible to request a settlement?**

You can apply for a settlement if you have a petition for redetermination, a late protest, or a claim for refund pending before the Board. To be considered, your settlement proposal must be submitted at least 30 days before the first scheduled Board hearing on the matter.

*Note:* If you apply for a settlement, you must continue to meet all applicable deadlines for your petition for redetermination or claim for



refund. If your case is not accepted, or no agreement is reached, your appeal will continue through the normal appeals process.

### How do I apply?

To request a settlement, submit a signed and dated written request that includes the following information:

- Your name and current address
- If applicable, the name, address, fax and phone number of your representative, as well as a copy of the representative's power of attorney
- Your taxpayer or feepayer account number
- Tax or fee period involved
- Type of tax or fee involved (such as, sales tax, use tax, or diesel fuel tax)
- A good faith settlement offer, including factual and legal grounds in support of the offer

Send your request to

Assistant Chief Counsel  
Settlement and Administration Section  
Legal Division  
P.O. Box 942879  
Sacramento, CA 94279-0087

After reviewing your request and evaluating the risks and costs associated with the litigation of these matters, settlement staff will advise you or your representative whether the case will be accepted into the settlement program. If staff determines that there is a legitimate factual or legal dispute, a case generally will be accepted. However, staff may reject your proposal for a variety of reasons. For example, if you do not provide enough facts in support of your case, the case will not likely be accepted.

If your case is accepted for consideration, staff will evaluate your offer and may accept or reject it. If appropriate, staff may seek to negotiate an agreement to a different amount. If your case is not accepted, or no agreement is reached, your appeal will continue through the normal appeals process. If you and staff reach a tentative agreement, you must sign a formal document setting

forth the terms of the agreement. The agreement will then be submitted for approval. If the settlement is approved, generally you will be expected to pay the agreed-upon amount within 30 days. When the agreement is executed on behalf of the Board, the settlement will become final and may be appealed only upon a showing of fraud or misrepresentation of a material fact.

If you would like additional information on settlements, you may visit our website at [www.boe.ca.gov/boe393n.htm](http://www.boe.ca.gov/boe393n.htm). Or call our Information Center and request a copy of publication 17, *Appeals Procedures*.

### 3. New Reporting Method Available to Drop Shippers

In general, drop shipment transactions involve two separate sales involving three persons:

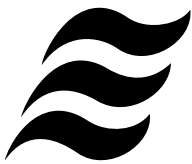
- The consumer in California who receives the property,
- The true retailer who sells the property *to the consumer* in California, and
- The drop shipper who sells the property *to the retailer*, but ships the property directly to the consumer in California on behalf of the true retailer.

If you are a drop shipper, as described above, you are generally liable for tax measured by the retail selling price of the property paid by the California consumer to the true retailer if

- The retailer is not engaged in business in California, and
- The retail sale of the property is subject to California sales or use tax.

Because it is difficult for drop shippers to determine the retail selling price to the consumer in California, Regulation 1706, *Drop Shipments*, was adopted.

Beginning January 1, 2001, Regulation 1706 provides that, for sales and use tax reporting purposes, a drop shipper may calculate the retail selling price of its drop shipments of property based on its selling price of the property to its direct customer, plus a mark-up of 10 percent.



A drop shipper may use a mark-up percentage lower than 10 percent if the drop shipper can document that the lower mark-up percentage accurately reflects the retail selling price charged to the California consumer.

If a mark-up percentage lower than 10 percent is developed in an audit of the drop shipper, the drop shipper may use that percentage for the subsequent reporting periods—provided the drop shipper has not had a significant change in business operations. Provided there is no significant change in business operations, if a later audit develops a higher percentage, the Board would not assess additional tax based on the newly computed mark-up percentage. For subsequent reporting periods, the drop shipper must use the higher percentage developed in the audit, or 10 percent, whichever is less.

*Note:* The provisions of Regulation 1706 for calculating the retail selling price of drop shipments for reporting purposes do not apply to drop shipments of vehicles, vessels, and aircraft (also known as courtesy deliveries).

If you have any questions regarding this revision or would like a copy of the new regulation, please call our Information Center.

#### **4. Sales by Social Clubs and Fraternal Organizations**

“Social Clubs and Fraternal Organizations” include any association or group acting as a unit, such as service clubs, lodges, and community, country, and athletic clubs. In general, sales made by these organizations *are* subject to tax even though the proceeds from routine and fund-raising sales may be used for charitable purposes. However, as explained below, certain food sales may not be taxable.

##### **Does tax apply to sales of meals, food, and drink?**

Although sales of food products are generally not subject to tax, tax may apply when the food products are sold as served meals, hot prepared food products, or at places where admission is charged.

Regulation 1603, *Taxable Sales of Food Products*, however, does provide that sales of meals, food, and drink by social clubs and fraternal organizations are not taxable if *both* of the following requirements are met:

- The meals, food, and beverages are sold *exclusively* to members, and
- They are sold less frequently than once a week.

If your organization furnishes meals to nonmembers or to a combination of members and nonmembers, tax applies to *all* receipts from the sale of meals, food, and drink.

*Note:* Meals, food, and drink paid for by members are considered furnished to members, even though consumed by guests who are not members.

##### **My group has a seller's permit. Do we really need one?**

Generally, if you make sales subject to sales tax in California, you are required to register as a seller and to hold a seller's permit. If your organization conducts *more than three* fund-raising sales events each year, or if your taxable sales activities occur continuously, you should hold a regular seller's permit. If your organization holds *no more than three* fund-raising events with taxable sales each year, you may apply for a temporary seller's permit for each event, instead of a regular seller's permit.

For more information about how tax applies to your organization's sales of food and other items, you may wish to obtain a copy of our publication 18, *Tax Tips for Nonprofit Organizations*.

#### **5. Clarification: Relief of Late Payment Penalty on Installment Payment Agreements**

In our December 2000 *Tax Information Bulletin*, we included an article summarizing new legislation regarding relief of late payment penalties on installment payment agreements. There has been some confusion about who is eligible for relief under the law change. The Sales and Use Tax Law now provides that, except in case of fraud, if a



person enters into a written installment payment agreement with the Board within 45 days of the date the Board's Notice of Determination or Redetermination becomes final, the taxpayer will be relieved of the late payment penalty, provided the taxpayer satisfactorily completes the installment proposal. *Note:* The relief of penalty provisions apply only to situations where the Board determines the amount of tax you owe. They do not apply to liabilities that result when you file your returns without making a full payment.

If you think you may qualify for relief, please call your local Board office for assistance.

## 6. Tax Liability of Corporate Officers or Shareholders of Suspended Corporations

The recently approved Regulation 1702.6, *Suspended Corporations*, clarifies when a corporate officer or shareholder of a suspended, closely held corporation is personally liable for sales or use tax liabilities incurred during the suspension period. Under California law, normal operations of a corporation stop until a suspension is lifted and corporate powers, rights, and privileges are restored. As a result, sales or purchases during a suspension period are not made by the corporation, but instead by the corporate officers or shareholders who operate the business. Those corporate officers or shareholders with control over operations or management may be liable for any sales or use tax incurred by the business during the suspension period.

As defined by Regulation 1702.6, a "closely held corporation" is a corporation in which the stock ownership is concentrated in one individual, one family, or a small number of individuals, **and** the majority stockholders manage the business.

The regulation defines "control over operations and management" as the power to affect day-to-day operations of the business. If you are a corporate officer of a closely held corporation, it is rebuttably presumed that you have this control.

If you are a corporate officer or shareholder and you have operated a closely-held corporation

during a suspension period, you may be liable for tax if, during this period, you did not report and pay tax on

- Sales of tangible personal property on which you collected sales or use tax
- Purchases of tangible personal property that you stored, used or consumed

Even though a corporate officer or shareholder may be liable for any unreported sales or use tax, the suspended corporation is equally liable for the unreported tax. That is, the Board can issue billings to both the corporation and the officers or shareholders.

If you have any questions about this new regulation or would like a copy, please call our Information Center. To download a copy from the Internet, visit [www.boe.ca.gov/staxregs.htm](http://www.boe.ca.gov/staxregs.htm).

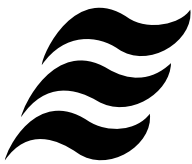
## 7. New Investigations Division

*To effectively combat tax evasion in California, the Board has consolidated its various investigation units into a single Investigations Division. — Editor*

The Investigations Division administers the Board's criminal investigations program. The Division plans, organizes, directs, and controls all criminal investigative activities for the various tax programs administered by the Board. Its goals are to identify tax evasion problems, recommend solutions to address those problems, identify new fraud schemes, and actively investigate and assist in the prosecution of crimes committed by individuals who are violating the laws administered by the Board.

Evasion can take place in any of the tax programs administered by the Board. Some examples of evasion include:

- Retailers and others who collect sales tax on sales but intentionally fail to report and pay the tax collected;
- Fuel retailers who blend waste petroleum products into gasoline or diesel and then sell the fuel as tax-paid but do not remit the taxes; and
- Retailers who sell untaxed cigarettes, untaxed tobacco products, or cigarettes that are



labeled "U.S. Tax Exempt, For Export Only" or are affixed with counterfeit tax stamps.

The penalties for evasion vary with the tax program. Persons convicted of felony tax evasion are subject to a fine of \$5,000 to \$20,000, or imprisonment for 16 months, two years or three years, or both the fine and imprisonment at the discretion of the court.

If you suspect fraudulent activity, or believe a business should be reporting taxes and is not, you may call the Investigations Division at 916-324-0105; call our Tax Evasion Hotline at 1-888-334-3300; send a fax to the division at 916-324-1578; or write to:

Investigations Division  
Board of Equalization  
P.O. Box 942879  
Sacramento, CA 94279-0042

## 8. Many Publications are Available in Spanish, Chinese, Korean, and Vietnamese

To serve the needs of California's diverse business community, the Board of Equalization translates some of its most popular publications. Titles such as *Your California Seller's Permit*, *The California Taxpayers Bill of Rights*, and *Guide to Board of Equalization Services* are available in Chinese, Korean, Spanish and Vietnamese. These and other translated publications may be obtained from your local field office, the Information Center, or our website at [www.boe.ca.gov/transpubs.htm](http://www.boe.ca.gov/transpubs.htm).

## 9. Your Rights as a Taxpayer

As a taxpayer, you have many rights under the Sales and Use Tax Law. These include the right to

- Know how the law affects you
- Be treated fairly, courteously, and promptly
- Question those actions and decisions of Board staff members and officers that affect your business operations

Of course, along with those rights, you have certain responsibilities, including the responsibility to

- Keep informed about tax laws and regulations

- Report and pay taxes when due
- Maintain adequate records of your business operations

For information on your rights as a taxpayer, you should order publication 70, *The California Taxpayers' Bill of Rights*. We also publish many other booklets that explain how to apply sales and use taxes. These publications include general information pamphlets and single-sheet *Tax Facts*, as well as *Tax Tips* pamphlets for specific types of businesses. A complete listing of our publications can be found in publication 51, *Guide to Board of Equalization Services*.

To request a publication, call our Information Center at 1-800-400-7115 and speak to a representative or leave a recorded message telling us where to mail you a copy. Many publications, including publications 51 and 70, are also available on the Internet at [www.boe.ca.gov](http://www.boe.ca.gov).

## 10. Change in the Application of Tax to a "Series of Sales"

Regulation 1595, *Occasional Sales – Sale of a Business – Business Reorganization*, was recently revised to clarify the application of tax to sales requiring a seller's permit. Generally, if you make more than two sales in a 12 month period, you are required to hold a seller's permit regardless of whether the sales were at retail, for resale, or exempt from tax (for example, a sale to the U.S. Government).

Under the previous application of tax, all of the nonexempt sales at retail in the series of sales were subject to tax. The revised regulation now considers the first two sales in the series of sales requiring you to hold a seller's permit, as occasional sales and therefore not subject to tax. As a result, only your third sale in the series and subsequent sales are subject to tax.

### For More Information

If you have any questions regarding this revision or would like a copy of the new regulation, please call our Information Center. To download a copy from the Internet, visit [www.boe.ca.gov/staxregs.htm](http://www.boe.ca.gov/staxregs.htm).



## 11. Where Do “Local Taxes” Go?

Did you know that the one percent “local tax” portion of the sales and use taxes you pay goes to local city and county governments? In fact, in fiscal year 1999-00, approximately \$4.1 billion dollars in local tax revenues were returned to the state’s 58 counties and 475 cities.

To ensure that each local jurisdiction receives its correct share of local tax, we must have your correct business address and business type on file. If you enter into a new type of business, move to a new business address, or add a new location, please let your local Board office know. When the local tax is distributed correctly, we all benefit.

## 12. Application of Tax to Purchases of Aircraft Outside California

Regulation 1620, *Interstate and Foreign Commerce*, was recently revised to clarify the application of tax to purchases of aircraft outside California.

The revised regulation establishes guidelines for determining whether an aircraft purchased outside this state is purchased for use in California (use tax applies to the use of an aircraft purchased for use in California unless a specific exemption applies). An aircraft is regarded as purchased for use in this state if it is first functionally used in California (that is, used for the purposes for which it was designed). If the aircraft is first functionally used outside California, it is nevertheless presumed to have been purchased for use in California if it is brought into this state within 90 days of purchase, excluding time of shipment and storage for shipment.

The revision to the regulation explains how you may overcome this presumption. You will not be regarded as having purchased the aircraft for use in California, and you will not be liable for California use tax, if *either* of the following conditions is met for the six-month period immediately following the aircraft’s entry into California:

- The aircraft is used or stored outside California one-half or more of the time; *or*

- One-half or more of the flight time traveled by the aircraft is commercial flight time traveled in interstate commerce.

### Other Changes

Regulation 1620 provides that there is no distinction made between the miles in an interstate or foreign commerce trip traveled by the aircraft in California versus the miles traveled in another state or country – all miles on a qualifying interstate trip are considered interstate commerce miles.

The examples in the regulation have also been revised to illustrate the types of activities that constitute use in interstate or foreign commerce for aircraft.

If you have any questions regarding this revision or would like a copy of the new regulation, please call our Information Center. To download a copy from the Internet, visit [www.boe.ca.gov/sitemap/regsitemap.htm](http://www.boe.ca.gov/sitemap/regsitemap.htm).

## 13. New Sales Tax Prepayment Rates for Distributions of Qualifying Fuels

Beginning April 1, 2001, the following prepayment rates will apply to distributions of gasoline, diesel, and other qualifying fuels:

- 9.5 cents (\$0.095) per gallon for motor vehicle fuel (gasoline)
- 5.0 cents (\$0.05) per gallon for aircraft jet fuel
- 8.0 cents (\$0.08) per gallon for diesel and other qualifying fuels, as described below

Other qualifying fuels include kerosene, any type of flammable liquid sold as or marketed as diesel fuel, and home heating oil meeting industry specifications for diesel No. 1 or No. 2.

These rates are scheduled to remain in effect through March 31, 2002, unless the price of these fuels increases or decreases significantly, resulting in prepayments that consistently exceed or are significantly lower than the fuel retailer’s sales tax liability.



## **14. New Sales And Use Tax Exemption Certificate for Excise Taxes on Fuel Purchases**

Effective January 1, 2001, pursuant to Revenue and Taxation Code section 6245.5, if you are a qualified purchaser, you may issue an exemption certificate to your fuel vendor for the amount of sales tax on the federal excise tax imposed by section 4081 or 4091 of the Internal Revenue Code when a *portion* of the fuel you are buying will be used in a manner that entitles you to a direct refund or credit against your income tax for that federal excise tax. Prior to January 1, 2001, you could issue a certificate only when *all* the fuel would be used in a qualifying manner.

When you issue an exemption certificate, you are required to pay directly to the Board tax on the amount of the federal excise tax paid with respect to the fuel you do not use in a qualifying manner.

You may have already received a special notice explaining the new sales and use tax exemption certificate and identifying the specific circumstances when you are considered a qualified purchaser. If you did not receive the notice and would like more information, you can call our Information Center. To download a copy of the special notice and certificate, visit [www.boe.ca.gov](http://www.boe.ca.gov).

## **15. Change in the Collection Point for the Motor Vehicle Fuel License Tax to Occur Next Year**

Operative January 1, 2002, Assembly Bill 2114 (Stats. 2000, Ch. 1053) conforms the Motor Vehicle Fuel License Tax Law to the state Diesel Fuel Tax Law and Federal Fuel Tax Law by moving the collection point of the tax from the first distribution level to the refinery or terminal rack level. It also conforms the Motor Vehicle Fuel License Tax Law to the state Diesel Fuel Tax Law and Federal Fuel Tax Law with respect to definitions and exemptions. An article explaining its impact on retailers will be published in the September 2001 *Tax Information Bulletin*.

## **16. New or Revised Reference Material**

If you would like to obtain a copy of any of the following reference material, please call the Information Center. Copies of some publications can also be obtained from our website, [www.boe.ca.gov](http://www.boe.ca.gov).

### **Sales and Use Tax Publications**

- 44 Tax Tips for District Taxes (January 2001)
- 71 California City and County Sales and Use Tax Rates (January 2001)
- 62 Tax Tips for Locksmiths (January 2001)
- 114 Consignment Sales (January 2001)

### **New Translations**

- 76-K Audits (7-99) (Korean)
- 51-S Guide to Board of Equalization Services (11-99) (Spanish)

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## ***For More Information***

### **Information Center**

1-800-400-7115

*Telephone devices for the deaf*

1-800-735-2929 (TDD phone)

1-800-735-2922 (voice phone)

### **Internet**

[www.boe.ca.gov](http://www.boe.ca.gov)

### **Seller's Permit Verification**

Visit our website or call 1-888-225-5263.

### **Taxpayers' Rights Advocate**

Call toll-free, 1-888-324-2798.

### **Tax Evasion Hotline**

Call toll-free, 1-888-334-3300.

### **Legislative Bills**

[www.leginfo.ca.gov](http://www.leginfo.ca.gov)